

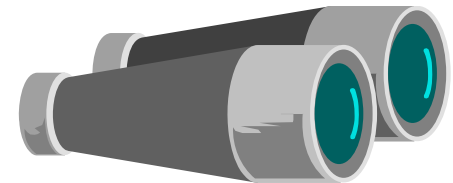
Banking Supervision and Regulation

**The Fed's Role, New Products and Credit
Protection**

November 2006

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Federal Reserve Bank of San Francisco





My Background

- ❑ Manager, Administrative Services Group
 - *Responsibilities include management of all examination support functions*

- ❑ Experience
 - Lending Officer/Branch Manager – 10 years
 - *Federal Reserve Bank – 18 years*
 - 12 years as a Consumer Compliance Examiner FRBSF
 - 6 years in training/examination support

Banking Supervision: Various Regulatory Agencies



The top section contains three logos. On the left is the DFI logo, which includes the text 'DFI' and 'Safety & Soundness' over a circular seal of the State of California. In the center is the seal of the Federal Reserve System, featuring an eagle and the text 'UNITED STATES FEDERAL RESERVE SYSTEM'. On the right is the FDIC logo, with 'FDIC' in large blue letters and 'Federal Deposit Insurance Corporation' below it, accompanied by a small circular seal.

State chartered banks



The middle section features a dark purple rectangular box with the text 'Comptroller of the Currency' and 'Administrator of National Banks' in white. To the right of the box is a red circular logo consisting of two interlocking shapes.

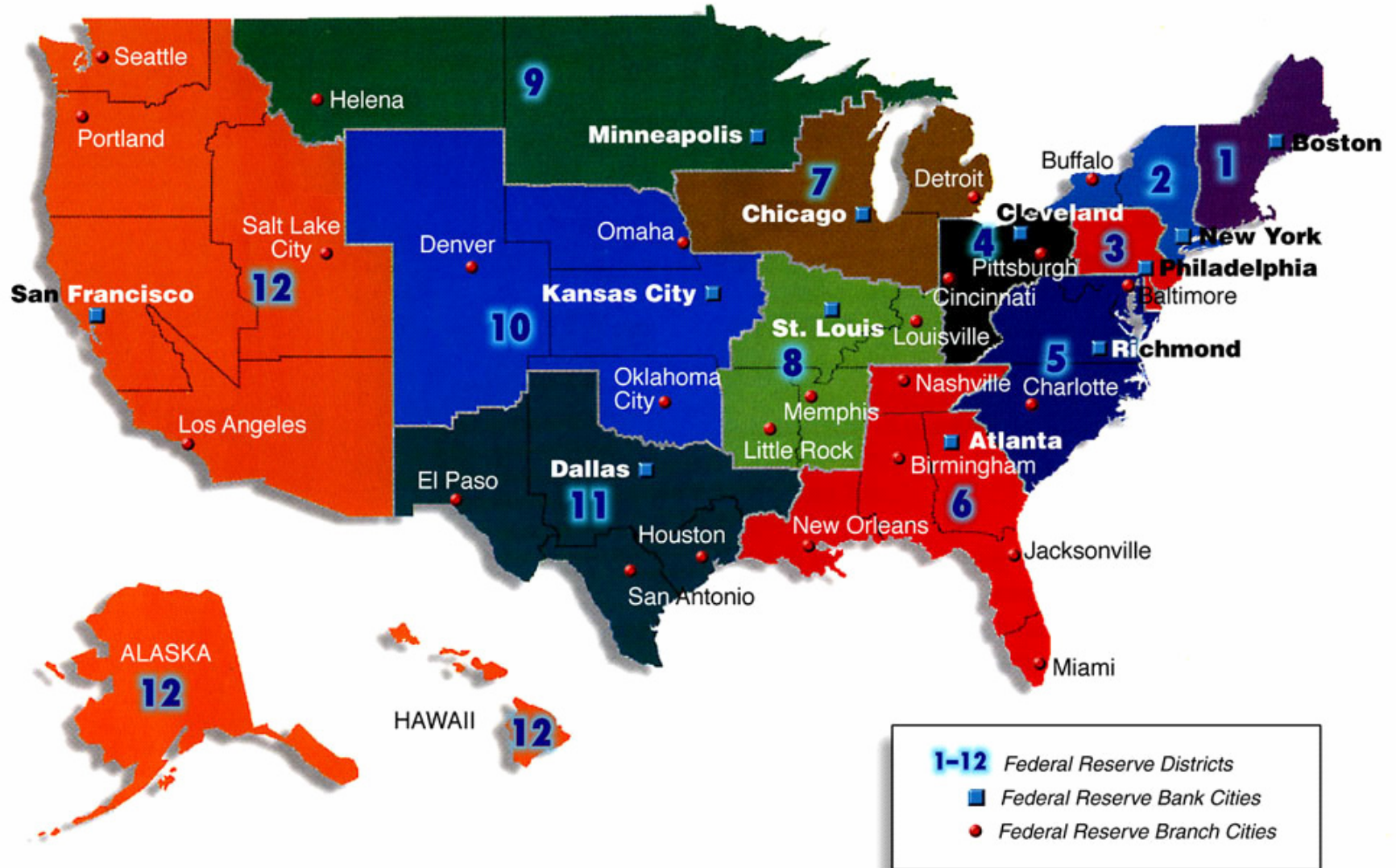
Nationally chartered banks



The bottom right section contains the seal of the Office of Thrift Supervision, which is circular and features a house icon with a red and white striped base, surrounded by stars and the text 'OFFICE OF THRIFT SUPERVISION' and '1989'.

Savings & Loans

Federal Reserve System





“Fed” Banking Supervision

Mission

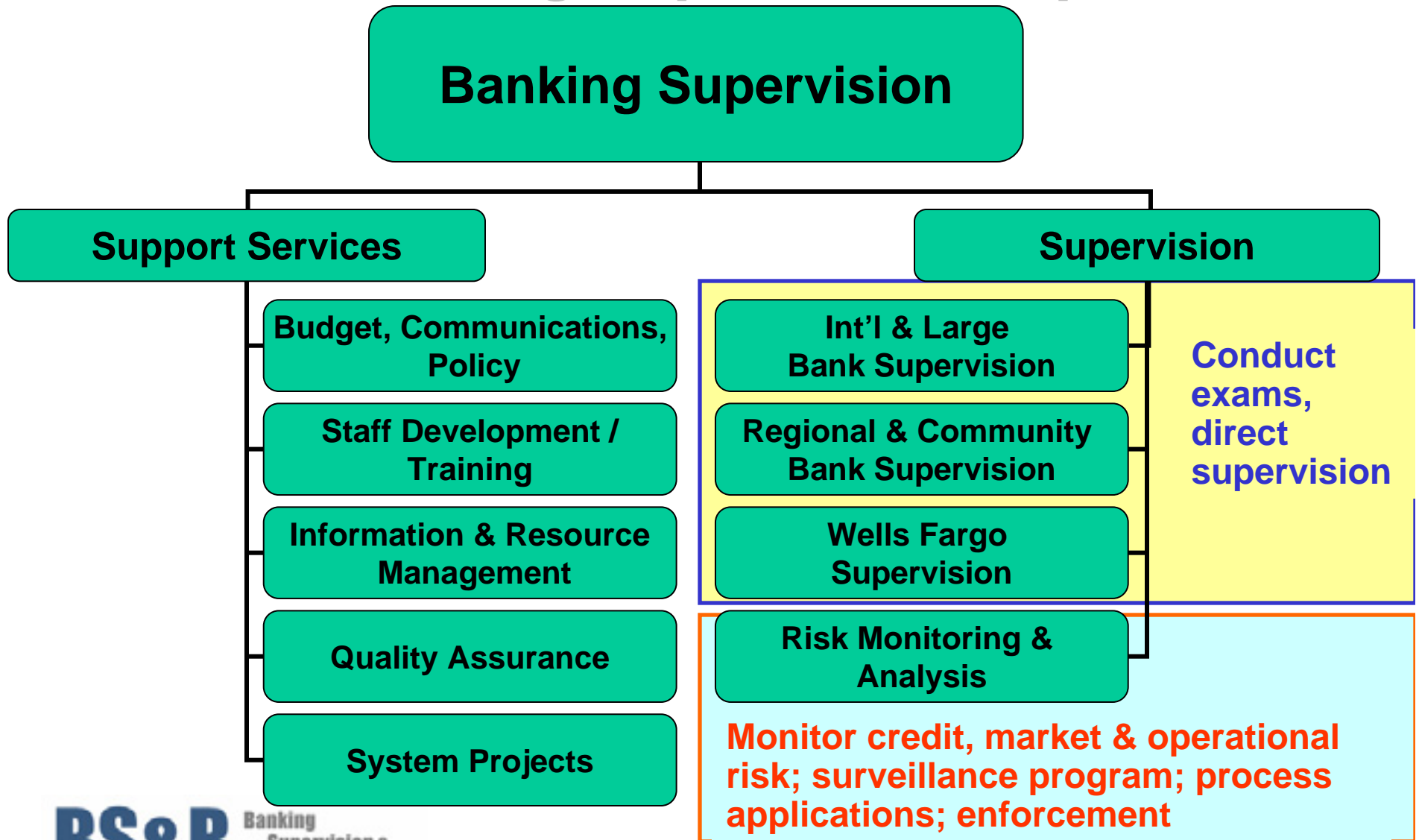
- ❑ Promote the safety and soundness of the banking system and compliance with laws and regulations

How?

- ❑ Conduct examinations of financial institutions (safety & soundness, regulatory compliance)
- ❑ Monitor performance and compliance off-site (early-identification of emerging risks)
- ❑ Process applications (mergers, acquisitions, etc.)

SF Fed - Banking Supervision Department

Banking Supervision



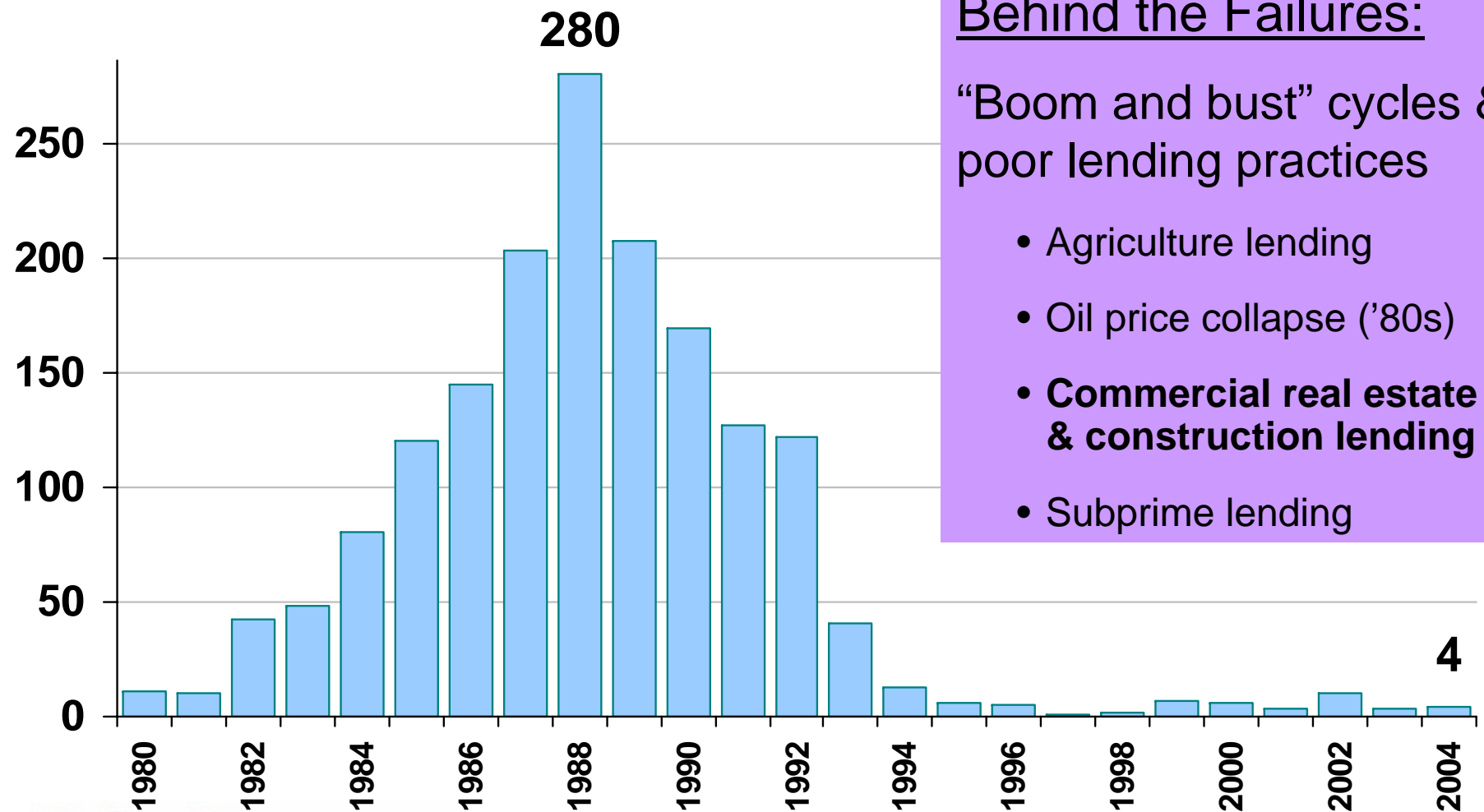
SF Fed's "Risk Assessment Council"

An inside perspective on bank supervisors' concerns



One Reason for Bank Supervisors' Concerns

Annual number of bank failures

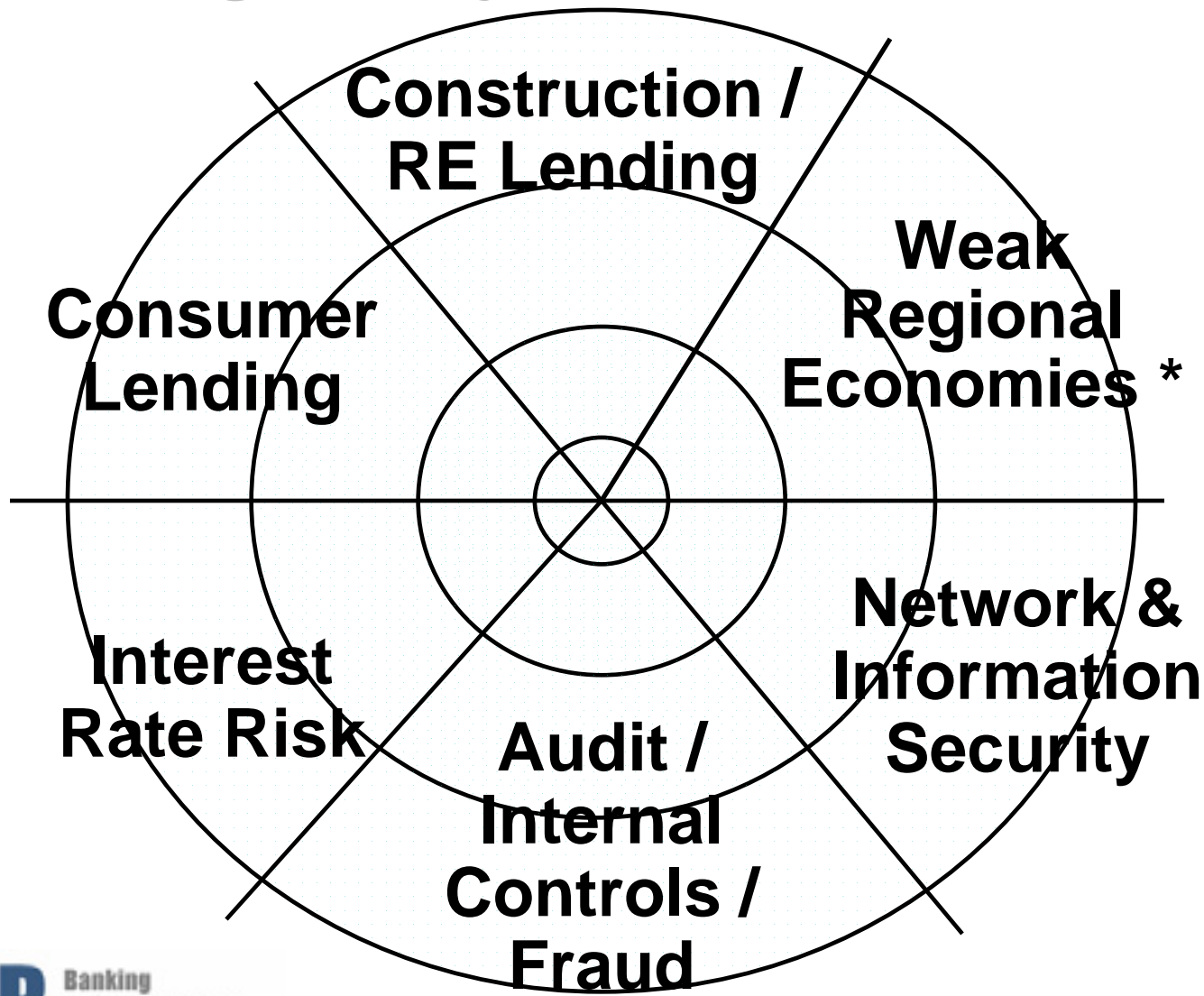


Behind the Failures:

“Boom and bust” cycles & poor lending practices

- Agriculture lending
- Oil price collapse ('80s)
- **Commercial real estate & construction lending**
- Subprime lending

Regulatory “Radar Screen”

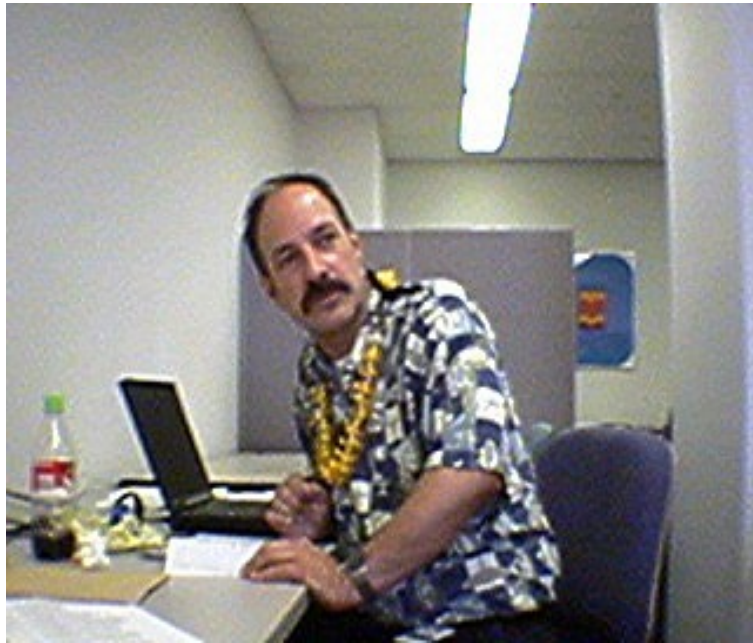


Real Estate / Construction Lending



- ❑ **Concentrations -**
high and increasing...
- ❑ **Real Estate Markets**
– will property values
stay strong or bust?

Consumer Lending *(includes residential & subprime)*



“He may not dress well, but he’s never missed a loan payment”

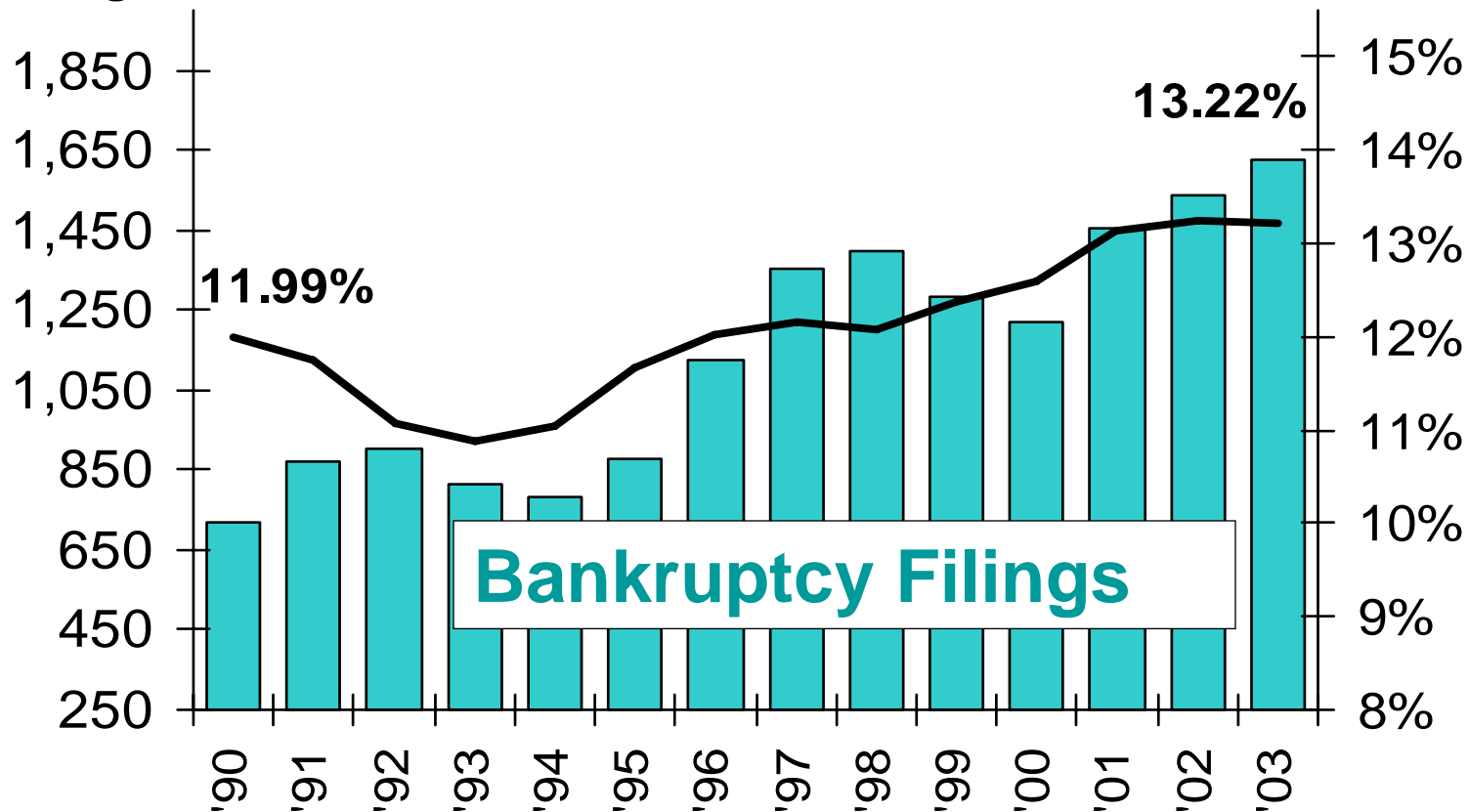
Reason for Caution:

- Weak economy**
 - high unemployment
 - high bankruptcy rates
 - low consumer confidence
- High consumer debt**
- Rapid growth of home loans (e.g. home equity lines)**
- Potential regional RE market bubbles**
- Subprime loan risks**

Consumer Lending Risks

Number of consumer filings in thousands

Debt service payments / disposable personal income



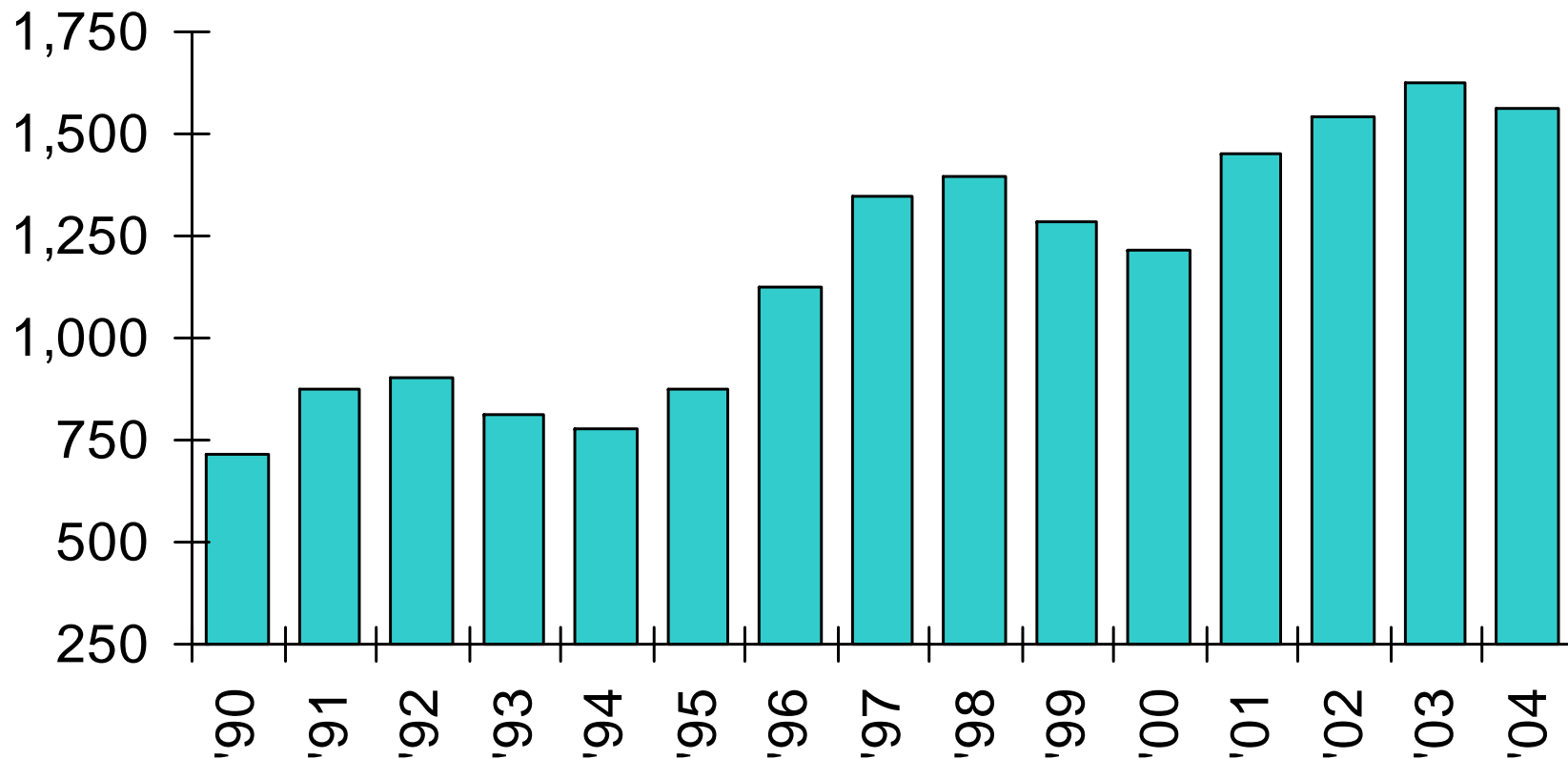
Bankruptcy Filings

Source: Federal Reserve Board; American Bankruptcy Inst.

II. Consumer Lending

Bankruptcy Filings

Number of consumer filings in thousands



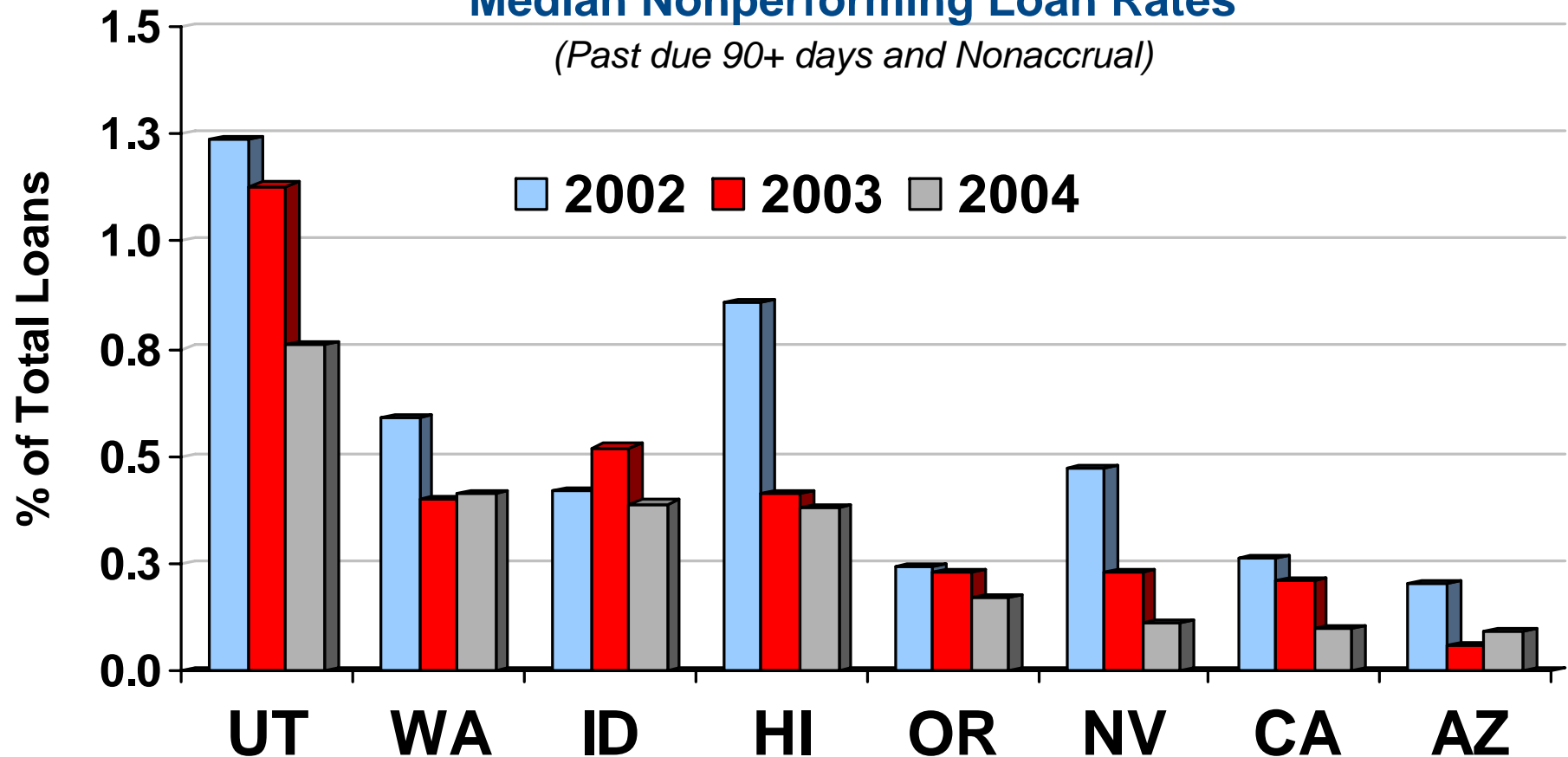
Source: American Bankruptcy Institute

Bank Loan Quality Continues to Improve

Utah banks have highest noncurrent loan rates, but levels improving rapidly

Median Nonperforming Loan Rates

(Past due 90+ days and Nonaccrual)



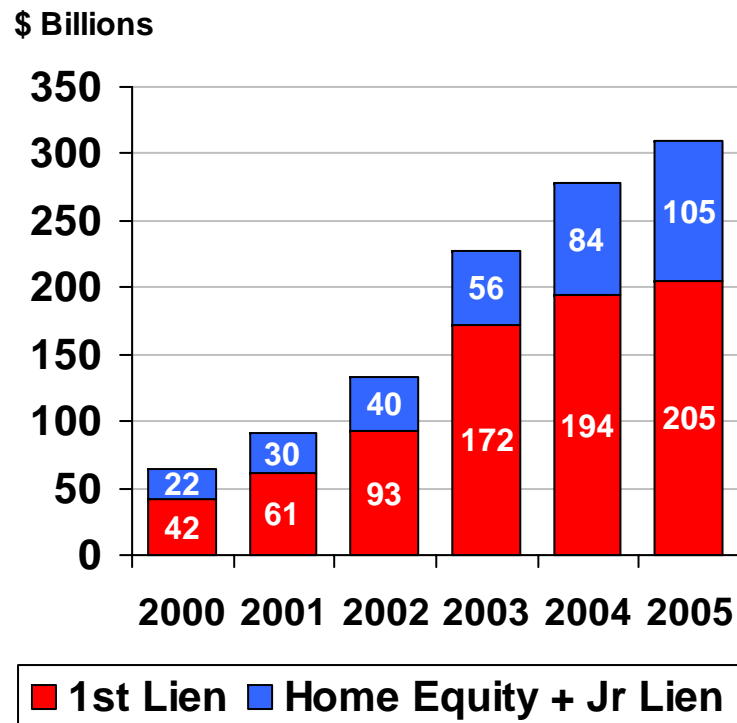
Banking
Supervision &
Regulation

Source: Bank Call Reports – Annual data are for the end of each year

II. Consumer Lending

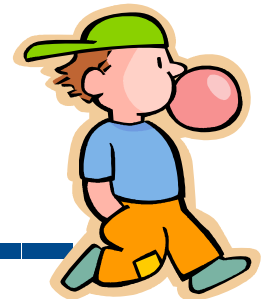
Consumer: Residential Lending Concerns

Total Residential Loans at
12th District Top Tier BHCs



Causes for Concern:

- Rapid growth of home lending, especially home equity lines
 - Home equity loans “are a time bomb” *
- Potential regional RE market bubbles

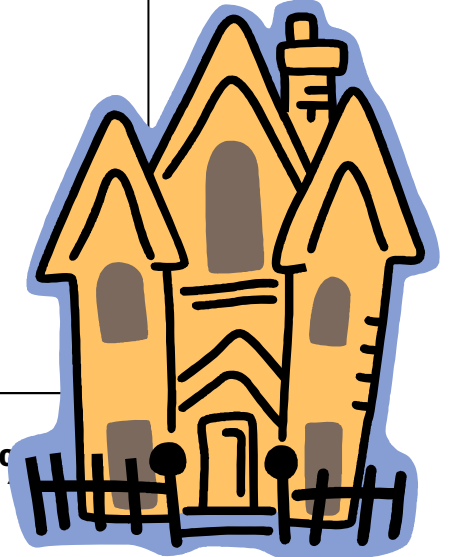
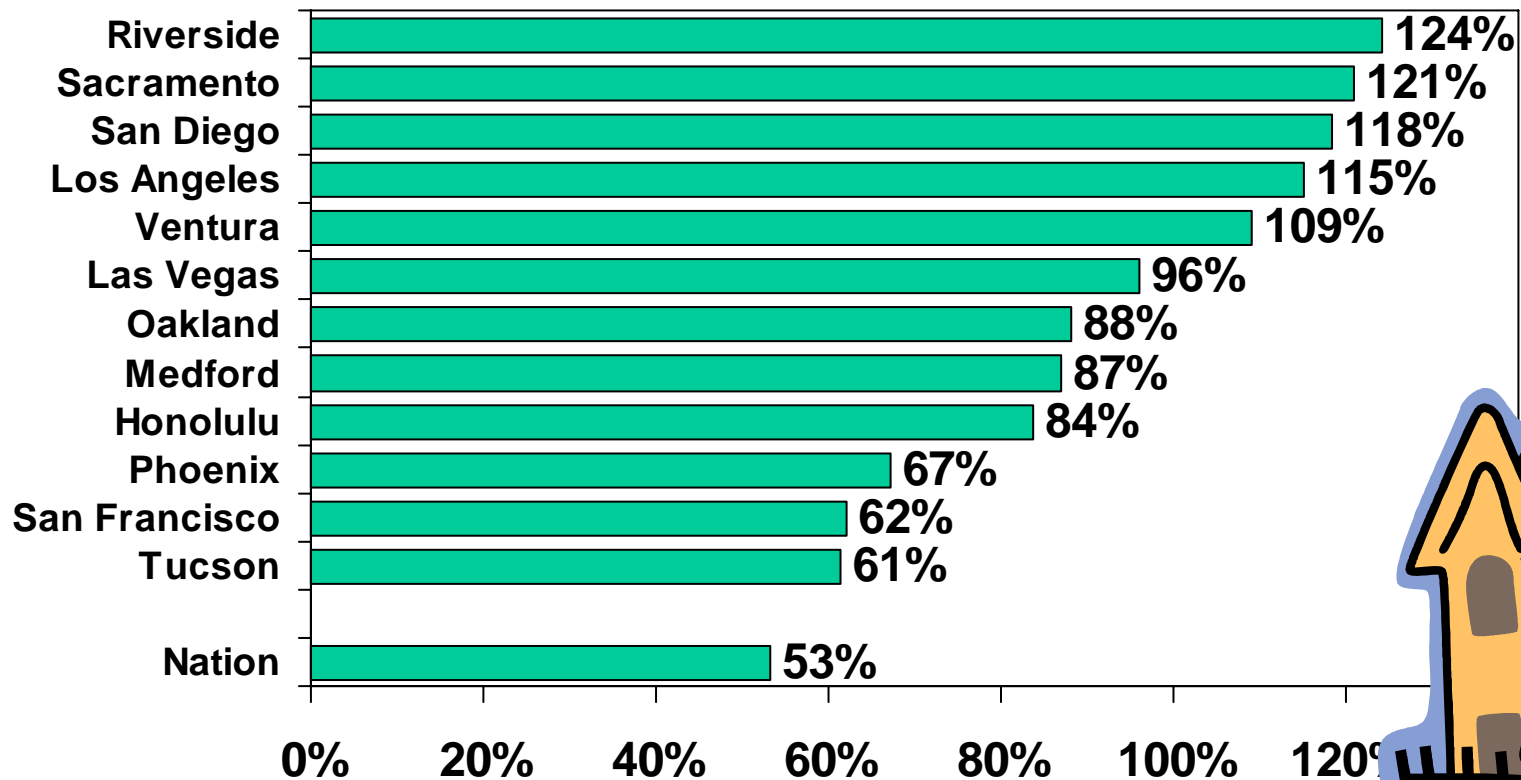


* Source of quote: Analyst Richard X. Bove

II. Consumer Lending

Rapid home price appreciation in some metro areas – sustainable?

5-Year home price index change from June 2000 to 2005 (%)



Conventional Mortgage Loan



Example: per \$100,000 at 5%

<u>10 year term</u>	<u>15 year term</u>	<u>30 year term</u>	
\$1,056	\$787	\$534	Per Month
\$126,720	\$141,660	\$192,240	Full Term

- A good example for term comparison is a \$500,000 loan at 5%

Compare how much you would pay over the life of the loan.

10 years = \$1,267,200

15 years = \$2,124,900

30 years = \$5,767,200

Riskier Mortgage Lending

- ❑ Option Arm

 - Regular Payment

 - Interest Only

 - Less than Interest Owed



- ❑ Payment Power

 - Minimal Payments

 - Skip Monthly Payments

 - Negative Amortization

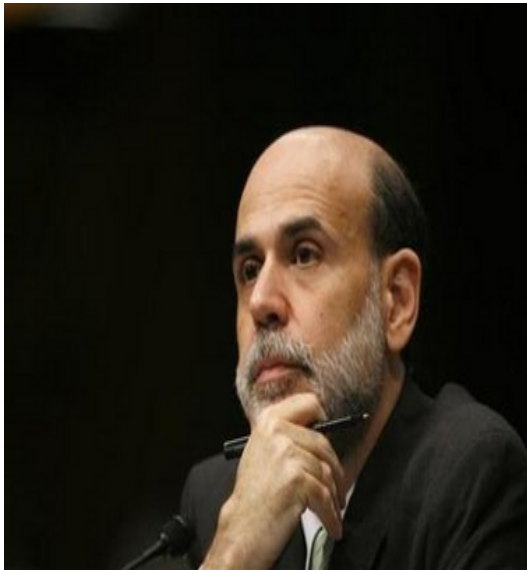
- ❑ Home Ownership Accelerator

 - Mortgage Married to Checking Account

Interest Only

Single-Family- Mortgage Loans 2004

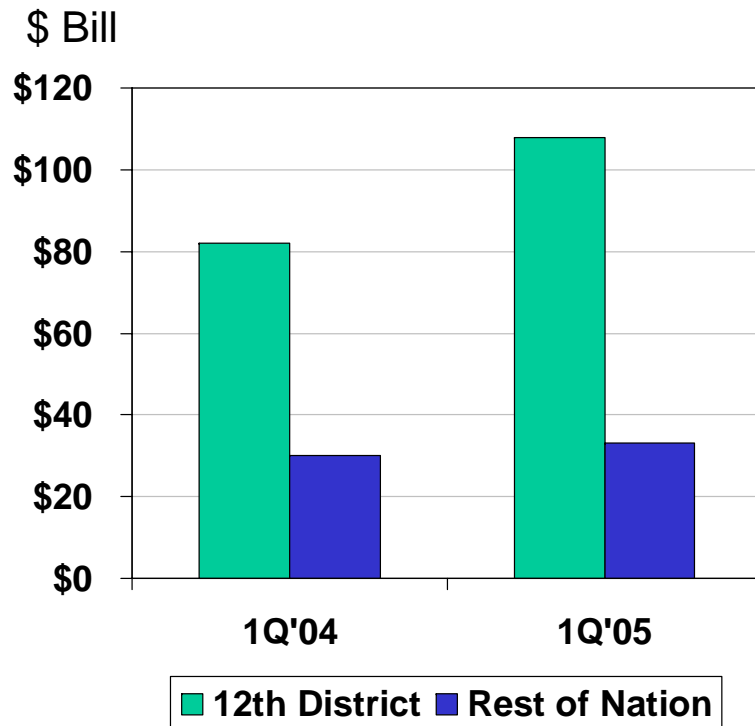
❑ San Diego	48%	(1.2% in 2001)
❑ Atlanta	46%	
❑ San Francisco	45%	
❑ Denver	43%	
❑ Oakland	43%	
❑ San Jose	41%	



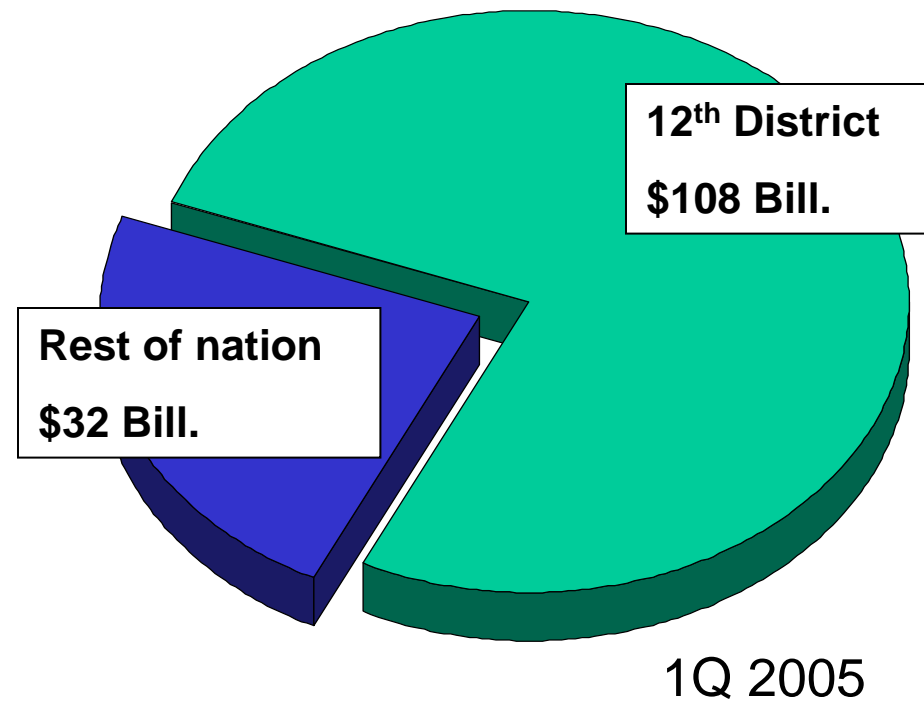
II. Consumer Lending

Consumer: Subprime Lending Risks

SF Fed District's Subprime Mortgage Lenders Grew 3 Times Faster Than Nation

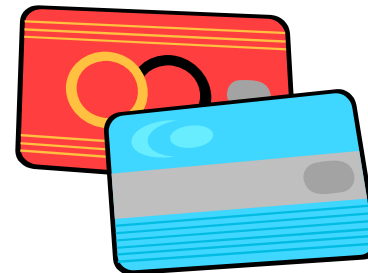


SF Fed District's Subprime Mortgage Lenders Account for 77% of Originations



Credit Card Debt

- ❑ The Average American Family owes over \$7,000 in credit card debt
- ❑ Monthly interest charges exceed \$105
- ❑ Making Minimum payments will take 29 years to pay-off this debt
- ❑ Making Minimum payments (\$20) at 18%
 - \$18,400 will be paid in interest on the \$7,000 debt



Consumer Protection



Issues:

- ❑ **Predatory Lending**
 - Fair Lending
 - Unfair and Deceptive Acts and Practices

- ❑ **Financial Privacy**
 - Identity theft
 - Fair and Accurate Credit Transactions (FACT) Act

V. Network & Information Security

Recent Headlines:

“Hacker Hits up to 8MM Credit Cards”

“Third Party Security: Who Can You Trust?”

“Corporate Losses to Cybercrime Increasing”

“46.9B is the amount of money lost annually by banks and other financial services providers due to the identity theft.”

“Human Error is Greatest Security Risk”



Summary: Banking Areas of Concern

The Federal Reserve Role



Consumer Lending



Consumer Protection



Information Security





Financial Educational - Web Cites

- ❑ www.frbsf.org/education/curriculum/index.html
- ❑ www.fdic.gov/consumers/consumer/moneysmart/index.html
- ❑ www.mymoney.gov
- ❑ www.thirteen.org/edonline/



Credit Reporting - Web Cites

- www.Experian.com
- www.Transunion.com
- www.Equifax.com
- www.annualcreditreport.com

Questions & Answers

